SUMMARY OF PRINCIPAL SHAREHOLDERS

The Company has completed two rounds of equity financing and one debt financing. In July 1998, Webley closed a $6 million Series A Preferred Stock offering with Patricof & Co. Ventures. In August 1999, the Company completed a $16.5 million Series B first closing with Forstmann Little & Co. and CSK Ventures, Inc. and also converted April 1999 bridge notes in the amount of $1.9 million. The Series B second closing occurred in April 2000 with a $16 million funding principally from America Online, Inc. and Net2Phone, Inc.

The following tables set forth certain information with respect to the effective ownership of Webley Systems common shares as of December 31, 2000, pro forma to reflect the proposed acquisitions of EffectNet and BuzMe.com. The Series D and Series E convertible preferred stock is assumed to be issued in consideration for the BuzMe.com and EffectNet acquisitions, respectively. In addition to the Series E convertible preferred stock, common stock will also be issued in consideration for the proposed EffectNet acquisition. Allocation of common stock and Series E convertible preferred stock in consideration of the EffectNet acquisition, as shown in the table below, is an estimate. (See "Recent Transactions")

Webley Ownership Table

Shareholder	Common Stock	Series A Preferred	Series B Preferred	Series D Preferred	Series E Preferred	Options	Reserved for Future Options	Total	Percent Beneficially Owned
EffectNet stockholders (1)	296,547				67,490			364,037	34.23%
APA Excelsior IV (2)		92,758	3,139			2,781		98,678	9.28%
Forstmann Little & Co.			76,704					76,704	7.21%
BuzMe.com stockholders (3)				52,350				52,350	4.92%
Vail Systems	50,000							50,000	4.70%
Mike Conners (4)			2,658			43,471		46,129	4.34%
Alex Kurganov (5)	32,500					8,000		40,500	3.81%
Patricia Mathis (5)			531			39,316		39,847	3.75%
Net2Phone, Inc.			38,352					38,352	3.61%
America Online, Inc.			38,352					38,352	3.61%
Hal Poel (5)	1,500		531			19,896		21,927	2.06%
Scot Thomas (2)	16,905		2,126			1,885		20,916	1.97%
Susan Kelley (5)	1,000		212			19,613		20,825	1.96%
Robert McConnell (5)						19,425		19,425	1.83%
Gary Kalanj (5)						9,714		9,714	0.91%
Others under 5%	42,204	1,822	13,902			39,679	28,200	125,807	11.83%
Totals	440,656	94,580	176,507	52,350	67,490	203,780	28,200	1,063,563	100.00%

(1) Series E Preferred and Common Stock to be issued upon the closing of the EffectNet acquisition
(2) Patricof & Co.
(3) Series D Preferred stock to be issued upon the closing of the BuzMe.com acquisition
(4) Member of Board
(5) Member of Management Team

DESCRIPTION OF CAPITAL STOCK

Authorized and Outstanding Capital Stock

The Company's authorized capital stock currently consists of 1,000,000 shares of common stock, par value $.001 per share (the "Common Stock"), and 280,231 shares of preferred stock, par value $.001 per share (the "Preferred Stock"). The Preferred Stock consists of two classes, the Series A Preferred Stock (the "Series A Preferred"), consisting of 94,580 shares, and the Series B Preferred Stock (the "Series B Preferred"), consisting of 185,651 shares.

Of the Preferred Stock, all 94,580 authorized shares of Series A Preferred, and 176,507 shares of Series B Preferred, are issued and outstanding. An additional 9,144 shares of Series B Preferred are reserved for issuance upon exercise of warrants. Of the Common Stock, 144,109 shares are issued and outstanding; 94,580 shares are reserved for issuance upon conversion of the Series A Preferred; 185,651 shares are reserved for issuance upon conversion of the Series B Preferred; and 222,836 shares are reserved for issuance upon exercise of options issuable to Company employees, consultants and directors (of which options to purchase 192,558 shares of Common Stock are outstanding).

The Company's capital structure will be materially changed upon the closing of its pending acquisitions of EffectNet and BuzMe.com. In order to optimize the tax structure for the acquisitions, Webley will adopt a new holding company organization. The new holding company, Webley Corporation, has formed three wholly owned, transitory subsidiaries for purposes of effectuating the restructuring. The acquisitions of EffectNet and BuzMe.com will occur contemporaneously via reverse subsidiary mergers with the transitory subsidiaries. At the same time, the Company will become a wholly owned subsidiary of Webley Corporation, also via a reverse subsidiary merger. As a result of these transactions, the Company, EffectNet and BuzMe.com each will become a wholly owned subsidiary of Webley Corporation, which will then change its name to "Webley Systems, Inc."

In connection with the restructuring, the stockholders of Webley Systems will exchange their existing Company securities for identical securities of Webley Corporation, the new holding company. Pursuant to the BuzMe.com acquisition, Webley Corporation will issue, on a fully diluted basis, approximately 52,350 shares of its Series D Preferred Stock (the "Series D Preferred") to BuzMe.com stockholders; and pursuant to the closing of the EffectNet acquisition, Webley Corporation will issue, on a fully diluted basis, approximately ____ shares of its Common Stock and ____ shares of its Series E Preferred Stock (the "Series E Preferred") to the former EffectNet Stockholders.

The following description of the Company's capital stock assumes the completion of the holding company formation and the EffectNet and BuzMe.com acquisitions in accordance with the terms of the existing acquisition agreements, and the "Company" refers to Webley Systems or Webley Corporation, as the context may require.

Rights and Preferences of Preferred Stock

Dividends and Distributions. The holders of the Series A Preferred are entitled to receive cumulative, quarterly dividends at the rate of $3.1825 per share per annum in cash or in kind (with each shares of Series A Preferred valued at $63.65), and the holders of the Series B Preferred are entitled to receive cumulative, quarterly dividends at the rate of $9.778 per share per annum in cash or in kind (with each shares of Series B Preferred valued at $195.56). The holders of the Series E Preferred are entitled to receive cumulative, quarterly dividends at the rate of $9.778 per share per annum in cash or in kind (with each share of Series E Preferred valued at $195.56), and the holders of the Series D Preferred are entitled to receive cumulative, quarterly dividends at the rate of $17.3832 per share per annum in cash or in kind (with each share of Series D Preferred valued at $347.664).

Liquidation Rights. The holders of the Series A Preferred are entitled to a liquidation preference of $63.65 per share, and the holders of the Series B Preferred are entitled to a liquidation preference of $195.56 per share. The holders of the Series E Preferred are entitled to a liquidation preference of $195.56 per share, and the holders of the Series D Preferred are entitled to a liquidation preference of $347.664 per share.

Conversion Rights. Each share of the Company's Preferred Stock is convertible at any time at the option of its holders, into one share of Common Stock (subject to customary adjustment provisions).

Each share of the Company's Preferred Stock will automatically convert into shares of Common Stock upon the occurrence of either of the following:

- In the case of the Series A Preferred, Series E Preferred and Series D Preferred, upon the request of the holders of a simple majority thereof; and in the case of the Series B Preferred, upon the request of the holders of a two-thirds majority thereof; or

- Upon the Company's completion of an underwritten initial public offering at an offering price of at least $190.95 per share, in the case of the Series A Preferred, and of at least $586.68 per share, in the case of the Series B Preferred, Series E Preferred and Series D Preferred, and in each case resulting in aggregate proceeds to the Company of at least $15,000,000 (a "Qualified Public Offering").

Voting Rights. Each share of Common Stock is entitled to one vote per share, and each share of Preferred Stock is entitled to a number of votes per share equal to the number of shares of Common Stock into which it is convertible (which is currently one). Holders of the Series A Preferred, Series B Preferred, Series D Preferred and Series E Preferred are entitled to a separate class vote on any proposed amendment to the Certificate of Incorporation that would adversely affect their rights and preferences. Holders of the Series A Preferred, Series B Preferred and Series E Preferred (but not the Series D Preferred) also are entitled to a separate class vote as to the creation of any new class of Preferred Stock having rights *pari passu* with or senior to the rights of such class.

The Certificate of Incorporation provides for a Board of Directors consisting of from six to nine directors, as fixed by the Board, and will be composed as follows:

- So long as at least 23,606 shares of Series A Preferred are outstanding, two directors selected by the holders of the Series A Preferred;

- So long as at least 34,678 shares of Series B Preferred are outstanding, two directors selected by the holders of the Series B Preferred;

- So long as at least 17,339 shares but less than 34,678 shares of Series B Preferred are outstanding, one director selected by the holders of the Series B Preferred;

- Two directors selected by the holders of the Common Stock; and

- The remaining directors, if any, will be elected by the holders of the Common Stock, Series A Preferred and Series B Preferred voting together.

In addition, the holders of the Series E Preferred, to be issued in the EffectNet acquisition, will have the right to designate one director prior to a Qualified Public Offering.

Investor Rights Agreements

1999 Investor Rights Agreement. The Company, the holders of the Series A Preferred and certain holders of the Series B Preferred are parties to an Investor Rights Agreement dated August 13, 1999 (the "1999 Investor Rights Agreement").

The 1999 Investor Rights Agreement grants two demand registration rights to the holders of the Series A Preferred and grants two demand registration rights to the holders of the Series B Preferred who are party to the agreement (collectively, the "1999 Investors"), subject to customary holdbacks and standoffs. The 1999 Investor Rights Agreement also grants the 1999 Investors unlimited piggyback registration rights, again subject to customary holdbacks and standoffs. The 1999 Investor Rights Agreement grants both the holders of the Series A Preferred and the holders of the Series B Preferred who are party to the agreement each two S-3 registration rights per annum (at such time as the Company is eligible to use such form). All these registration rights will terminate five years after the closing of an underwritten public offering of the Common Stock.

Pursuant to the 1999 Investor Rights Agreement, the Company grants the 1999 Investors a right of first offer with respect to further sales by the Company of shares of its capital stock. These rights will terminate when the Company completes a Qualified Public Offering.

Also pursuant to the 1999 Investor Rights Agreement, if at any time any 1999 Investor or certain other principal holders of the Common Stock wishes to sell any of its Company securities, the 1999 Investors are entitled to participate *pro rata* in the sale. Certain proposed transfers, including transfers for estate planning purposes, transfers to family members, sales pursuant to public offerings and transfers of less than 15% of a stockholder's ownership position, do not give rise to *pro rata* participation rights. These provisions will terminate when the Company completes a Qualified Public Offering.

2000 Investor Rights Agreement. On March 31, 2000, the Company entered into separate Investor Rights Agreements (the "2000 Investor Rights Agreements") with each of America Online, Inc. ("AOL") and Net2Phone, Inc. ("N2P") in connection with their respective purchases of shares of the Series B Preferred. Pursuant to these agreements, the Company grants AOL and N2P each one demand registration right, unlimited piggyback registration rights and one S-3 registration right per annum (at such time as the Company is eligible to use such form). These registration rights are subject to customary holdbacks and standoffs, and will terminate five years after the completion of an underwritten public offering of the Common Stock.

Pursuant to the 2000 Investor Rights Agreement, the Company grants AOL and N2P each a right of first offer with respect to future sales by the Company of shares of its capital stock. These rights will terminate when the Company completes a Qualified Public Offering.

Also pursuant to the 2000 Investor Rights Agreement, at any time AOL or N2P wishes to sell any of its Company securities, AOL or N2P (as the case may be) and the 1999 Investors are entitled to participate *pro rata* in the sale. Certain proposed transfers, including sales pursuant to public offerings and transfers of less than 15% of a stockholder's ownership position, do not give rise to the *pro rata* participation rights. The 1999 Investors and the other principal holders of the Common Stock have granted AOL and N2P corresponding rights to participate *pro rata* in sales of Company securities by them. These provisions will terminate when the Company completes a Qualified Public Offering.

The Series E Preferred will have a right of first offer, similar to the AOL and N2P rights. Finally, pursuant to the agreement to acquire EffectNet, Webley is obligated to use its reasonable efforts to negotiate in good faith customary investor rights agreements on behalf of the holders of Webley common stock.

RISK FACTORS

An investment in the Securities is speculative in nature and involves a high degree of risk. In evaluating the Company and its business, prospective investors should carefully consider the following risk factors. This Memorandum contains, in addition to historical information, forward-looking statements that involve risks and uncertainties. The Company's actual results could differ materially from the results discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed below as well as those discussed elsewhere in this Memorandum.

Webley Systems has a history of losses and expects to incur losses in the future.

Webley Systems has not been profitable since its inception in February 1997. For the years ended 1999 and 2000, Webley Systems had net losses of approximately $13.4 and $17.7 million, respectively. Webley Systems expects to continue to incur losses in the foreseeable future. It also anticipates that expenses will increase substantially in the foreseeable future as it continues to increase research and development, sales and marketing and general and administrative expenses. These efforts may prove more expensive than Webley Systems currently anticipates. Webley Systems cannot predict if it will ever achieve profitability and if it does, Webley Systems may not be able to sustain or increase its profitability.

Because Webley Systems has a limited operating history, it may be difficult for investors to evaluate the business and Webley Systems' future prospects.

Evaluating Webley Systems' business will be more difficult because of a limited operating history. Webley Systems was founded in February 1997. In December 1999, Webley completed its separation from Vail Systems and Webley became fully self-sufficient with operational functions of its own. Since Webley Systems is in an early stage of development, its prospects are difficult to predict and may change rapidly. When making an investment decision, you should consider the risks, expenses and difficulties that may be encountered or incurred as a young company in a new and rapidly evolving market, including substantial dependence on a product with limited market acceptance to date and a need to manage expanding operations. Webley Systems' business strategy may not be successful, and it may not successfully address these risks.

The market for Webley Systems' products and services is new and may have slower than anticipated adoption rates by its potential customers.

Webley Systems believes that its future business prospects depend on its customers accepting unified messaging as a means of accessing various forms of communications, and on its ability to maintain and improve current services and to develop new ones in a timely basis. Webley Systems' services will have to achieve market acceptance, maintain technological competitiveness and meet an expanding range of customer requirements. As a result of the complexities inherent in service offerings, Unified Communications services require long development and testing periods. Additionally, Webley Systems' potential customers may be reluctant or slow to adopt Unified Communications technology due to its complexity and potential risks. As a result, new services and service enhancements may not achieve market acceptance. If Webley Systems cannot effectively develop, improve, and generate market acceptance of its products and services, it may not be able to recover fixed costs or otherwise become profitable.

Webley Systems faces competition from existing and new competitors and from new products that could cause it to lose market share and cause its revenue to decline.

Intense competition could develop in the market for the services Webley Systems offers. Webley's technology architecture, which links communications devices with media through either voice or Web user interfaces, has been

designed from the beginning to be an open architecture. Webley System's competitors may use the same products and services in competition with it. With time and capital, it would be possible for competitors to replicate Webley Systems' services. In addition, competitors may market their products and services more effectively than Webley Systems does, which could decrease demand for its product and cause its revenue to decline. Webley Systems may also face competition in the future from established companies who have not previously entered the market for Unified Communications services. Webley Systems' competitors could include large infrastructure players, voice portals, and wireless handset and PDA service providers. It is possible that new competitors or alliances among competitors may emerge and rapidly acquire significant market share. In addition, many of Webley Systems' competitors have greater resources, which may enable them to penetrate the market more quickly.

If Webley Systems does not have sufficient capital to fund its operations, it may be forced to discontinue product development, reduce sales and marketing efforts or forego attractive business opportunities.

Webley Systems may not have sufficient capital to fund its operations and additional capital may not be available on acceptable terms, if at all. Any of these outcomes could adversely impact the ability to respond to competitive pressures or prevent it from conducting all or a portion of its planned operations. Even if the Company raises all of the expected net proceeds sought in this offering, the Company will be required to raise additional funds to carry out its business plan. Webley Systems may also require additional capital to acquire or invest in complementary businesses or products or obtain the right to use complementary technologies. If Webley Systems issues additional equity securities to raise funds, investors' ownership percentage in Webley Systems will be reduced.

The Company faces risks associated with the expansion of its sales force and its distribution infrastructure.

To date, the Company has sold its services primarily through its direct sales force and certain resellers. The Company's future revenue growth will depend in large part on recruiting and training additional direct sales and indirect sales personnel and expanding its distribution channels. The Company may experience difficulty in recruiting qualified sales and support personnel and in establishing third-party relationships. The Company may not be able to successfully expand its direct sales force or other distribution channels and any such expansion may not result in increased revenues. The Company's business, financial condition and operating results will be materially adversely affected if it fails to expand its direct sales force or other distribution channels.

Webley Systems may fail to support its anticipated growth in operations which could reduce demand for its services and materially adversely affect its revenue.

Webley Systems' business strategy is based on the assumption that the number of subscribers to its services and the number of services the Company will offer will both increase. Webley Systems must continue to develop and expand its services and operations to accommodate this growth. The expansion of the Company's area of service and development of its communications platform requires substantial financial, operational and management resources. Webley Systems may be unable to expand its operations for one or more of the following reasons:

- Webley Systems may not be able to locate or hire at reasonable compensation rates qualified engineers and other employees necessary to expand its capacity;
- Webley Systems may not be able to form the necessary strategic partnerships to expand its business; and
- Webley Systems may not be able to expand its customer support and other related support systems.

Due to the limited deployment of Webley Systems' services to date, the ability of its systems and operations to sustain a substantially larger base of subscribers while maintaining superior performance is unknown. Any failure on Webley Systems' part to develop and maintain its Unified Communications services as Webley Systems experiences rapid growth could significantly reduce demand for its services and materially adversely affect revenue.

Webley Systems financial projections rely in part upon per minute usage pricing for its products and services. If Webley Systems is unable to substantially achieve the number of subscribers and minutes of usage for its products as projected, it may be unable to generate the increased revenue necessary to achieve profitability. Similarly, if Webley Systems is unable to negotiate the projected per minute cost for minutes resold to its customers from the service providers with which it contracts, the Company may not be able to meet its revenue and cost of sales and, therefore, associated margins as presented in this Memorandum.

A substantial portion of Webley Systems' revenue is derived from per minute usage pricing on the resale of telecommunications service which has been provisioned with the Webley services as described in this Offering Memorandum. Webley has based its projections with regards to the per minute usage pricing set forth herewith on its current and previous implementation field experience. Webley believes that these estimates represent an appropriate basis from which to project the Company's financial estimates. However, Webley cannot make assurances you that it will achieve the growth in subscribers or minutes of usage with which the Company has based its projections. Additionally, the Company's inability to achieve the estimated pricing from the telecommunications service providers for minutes resold to its customers, or the estimated per minute pricing in resale, could adversely affect the Company's results of operations and decrease sales, increase cost of sales or both. This, in turn, could have an adverse effect on the estimated margins associated with per minute usage revenue as projected in this Memorandum.

Since Webley's software products and service platforms are complex, there are likely to be undetected errors or defects, especially when first introduced or when new versions are released.

Webley has in the past experienced delays in releasing some versions of its services until software problems were corrected. Webley's services may not be free from errors or defects after commercial deployment is begun, which could result in the rejection of its services and damage to its reputation, as well as lost revenues, diverted development resources, and increased service and warranty costs, any or all of which could harm Webley's business.

Security problems in the Company's voice application services or products would likely result in significant liability and reduced revenues.

Security vulnerabilities and weaknesses may be discovered in the Company's voice application services or products, in the licensed technology incorporated in the Company's voice application services or products, in the Company's network operations center hosting environment, or in the media by which end users access the Company's voice application services or products. Any such security problems may require the Company to expend significant capital and other resources to alleviate the problems. In addition, these problems could result in the loss or misuse of users' personal information, and may limit the number of customers or subscribers for the Company's voice application services or products. A decrease in the number of customers could lead to decreased revenues. These problems may also cause interruptions or delays in the development of enhancements to the Company's voice application services and products and may result in lawsuits against the Company.

The Company will continue to incorporate security technologies in its voice application services and products. However, such technologies may not prove to be adequate. In addition, weaknesses in the media by which users access the Company's voice application services and products, including the Internet, land-line telephones, cellular phones and other wireless devices, may compromise the security of the electronic information accessed. The Company intends to continue to limit its liability to end users and to our customers and partners, including liability arising from failure of the security technologies incorporated into its services and products, through contractual provisions. However, the Company may not successfully negotiate such limitations with all its customers and partners, nor may such limitations eliminate liability.

Webley Systems depends on recruiting and retaining key management and technical personnel with telecommunications and software experience and may not be able to develop new products or support existing products if it cannot hire or retain qualified employees.

Webley Systems' future success will depend in large part on its ability to recruit and retain experienced research and development, sales and marketing, customer service and management personnel. In particular, Webley Systems' future success depends in part on the continued services of its current executive officers. If it does not attract and retain such personnel, Webley Systems may not be able to grow its business. Competition for qualified personnel in the telecommunications and software industries is intense and finding qualified personnel with experience in both industries is even more difficult. In the past, Webley Systems has experienced difficulty in recruiting qualified personnel, especially technical and sales personnel. Webley Systems is in a new market and there are a limited number of people with the appropriate combination of skills needed to provide the services that its customers demand. Webley Systems expects competition for qualified personnel to remain intense, and it may not succeed in attracting or retaining sufficient personnel. In addition, new employees generally require substantial training, which requires significant resources and management attention.

If Webley Systems does not respond effectively and in a timely basis to rapid technological change, its services may become obsolete and it may lose sales.

The personal communications industry is characterized by rapidly changing technologies, industry standards, customer needs and competition, as well as by frequent new product and service introductions. Webley Systems' services are integrated with a variety of wireless devices. Webley Systems' services must also be compatible with the different communications platforms and protocols. Webley Systems must respond to technological changes affecting both its customers and suppliers. Webley Systems may not be successful in developing and marketing, in a timely and cost effective basis, new services that respond to technological changes, evolving industry standards or changing customer requirements. Webley Systems' ability to grow and achieve profitability will depend, in part, on its ability to accomplish all of the following in a timely and cost effective manner:

- Effectively use and integrate various communications platforms;
- Continue to develop its technical expertise in speech and character recognition technology;
- Enhance its personal communications services; and
- Influence and respond to emerging industry standards and other changes.

The failure or unavailability of third-party technologies and services could limit the Company's ability to generate revenues.

The Company relies and will continue to rely on technology developed by third parties for key voice application services and products offered to its customers. The Company has limited control over the timing or nature of enhancements to third-party technologies incorporated into its products and services. If a third party fails or refuses to timely develop, license or support technology necessary to the Company's services or products, market acceptance of the Company's services or products could be adversely affected. In addition, the Company's competitors may acquire interests in these third parties or their technologies, which may render the technology or certain enhancements unavailable to it.

Moreover, if these third-party technologies fail or otherwise prove not to be viable, the Company's ability to provide the Company's services and/or to generate revenues would be adversely affected. In addition, the Company relies and will continue to rely on telecommunications, Internet access, power and other services needed for the Company's network operations center. Market acceptance of the Company's services would be adversely affected if these third party services fail or are not reliable.

Webley's failure to develop recognition for the Webley Systems brand could prevent it from achieving a profitable level of sales.

Webley Systems' sales and marketing activities to date have been limited. For the years ended 1999 and 2000, Webley Systems' sales and marketing expenses were approximately $2.2 million and $4.5 million, respectively. Webley Systems intends to increase the market presence of its brand over time, which will require it to substantially increase the amount it spends on sales and marketing. Webley Systems expects to spend an estimated $9.6 million in 2001 on sales and marketing. Webley Systems may lose existing customers or fail to attract new customers if the Webley Systems brand is not well received by its customers, if its marketing efforts are not productive, if it is otherwise unsuccessful in increasing its brand awareness or if its competition has greater brand recognition.

If Webley fails to adequately protect its intellectual property rights or faces a claim of intellectual property infringement by a third party, Webley could lose its intellectual property or be liable for significant damages.

Webley's competitive advantage depends, in part, on certain domestic and foreign patent applications and certain copyrights, trademarks and trade secrets relating to its technology. Webley's success relies substantially on its ability to protect its proprietary technology, both domestically and abroad. Webley faces two major risks with its intellectual property rights:

1. Others may infringe on its intellectual property rights resulting in:
- Lack of competitiveness in the market;
- Expense of time and resources to protect its patent applications; and
- Dilution of the brand value of Webley service.

2. Although Webley does not believe this to be the case, Webley may infringe others' patents and other intellectual property, resulting in:
- Significant expense in defending technology, even in the case of a frivolous suit;
- Requirements to pay damages; and
- Costly and potentially impracticable redesign of its technology.

Webley may acquire technologies or companies in the future and these acquisitions could disrupt its business and dilute investors' holdings in Webley. Webley's pending acquisitions of EffectNet and BuzMe.com could encounter integration or execution problems and cause either operational or financial difficulties.

Webley Systems may acquire technologies or companies in the future. Entering into an acquisition entails many risks, any of which could materially harm its business, including:

- Diversion of management's attention from ongoing business concerns;
- Failure to effectively assimilate the acquired technology or company into its business;
- The loss of key employees from either its current business or the acquired business; and
- Assumption of significant liabilities of the acquired company.

Investor's holdings in Webley will be diluted if Webley issues equity securities in connection with any acquisition.

Additionally, Webley has entered into definitive agreements to acquire the businesses and assets of EffectNet and BuzMe.com. These acquisitions, if completed, will substantially increase the size of Webley's business in terms of employees, operations and revenues. Failure to successfully integrate these acquisitions, including any acquired technology or management, could result in substantial operational and financial difficulty for Webley and its shareholders.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF HISTORICAL FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS

Overview

Webley Systems is a recognized leader as a developer and provider of Unified Communication services to indirect and direct sales and marketing channels. Webley offers a carrier-grade solution and its proprietary, speech-enabled applications integrate Internet and telephony-based communications on its Unified Communications platform.

Webley was founded in 1997. Through 1997, Webley completed development and testing of its beta product version and began commercial sales and marketing in 1998. During the fourth quarter of 1998 Webley conducted direct market trials in the San Francisco area to refine user marketing strategies and acquire end user experience feedback. In 1999, Webley developed a local access market strategy to integrate Webley's service offering with existing telephone numbers of SOHO and small to medium business users. During 1998 and 1999, Webley revenues were primarily limited to toll free individual and corporate users. Beginning in the first quarter of 2000, Webley began a limited introduction of its local access strategy and expanded marketing activities in the greater Chicago area through a local Webley employed sales force. This local access campaign formed the foundation for the direct sales strategy contained in the forecasted financials.

During 2000 Webley began development of its next generation, communications platform utilizing SIP technology and VoIP data networks. Webley intends to shift future subscriber growth to this SIP platform through nationally deployed VoIP networks and soft switch gateways.

Revenues

Webley generates revenues from two principal sources: monthly service fees per subscriber mailbox and per minute usage fees for call volume on the Webley communications platform. Webley revenues include retail pricing to end users of Webley branded services and wholesale pricing, generally on a private label, to resellers of Unified Communications solutions. We are aggressively expanding both our direct sales force and our reseller and OEM relationships. Sales to our resellers and OEMs accounted for 10.5% of our total revenue for 1999 and 15.8% of our total revenue for 2000. We expect that revenue derived from sales to resellers and OEMs will continue to increase as a percentage of our total revenue for the foreseeable future as we focus on and expand our distribution channels.

Webley recognizes monthly fee revenue in the month earned and per minute usage revenue in the month usage occurs.

Webley markets its services principally in North America through our direct sales force, OEMs and value-added resellers such as BusinessMall.com and EffectNet. In 2000, BusinessMall.com represented 8% of revenues and EffectNet represented 4% of revenues. Webley expects EffectNet to represent over 70% of 2001 revenues, based on the consummation of the proposed acquisition. (See "Recent Transactions")

Cost of Revenues

Costs of revenues consist of local and long distance charges for call volume on the Webley communications platform, fixed monthly costs for dedicated network lines and co-location costs and credit card fees.

Operating Expenses

Selling and marketing expenses consist primarily of compensation and related expenses, sales commissions and travel expenses, along with other marketing expenses, including advertising, trade shows, public relations, direct mail campaigns, seminars and other promotional expenses. Research and development expenses consist primarily of compensation and related expenses for our personnel and, to a lesser extent, independent contractors, who work on new products, enhancements to existing products and the implementation of our products in new languages. General and administrative expenses consist primarily of compensation for our administrative, financial and information technology personnel, occupancy and overhead expense, and company-wide professional fees, including recruiting, legal and accounting fees, as well as bad debts. Stock compensation expenses result from non-cash charges for options issued with exercise prices that are less than the fair market value of our common stock on the date of grant.

Interest and Other Income (Expense)

We receive interest income by investing the proceeds raised in prior equity financings. Interest expense is generated primarily from amounts owed under lines of credit and capital lease obligations.

Income Taxes

Due to operating losses, no provision or benefit for income taxes is recorded for any period since inception. As of December 31, 2000, Webley had $31.3 million of net operating loss carryforwards for federal income tax purposes, which expire beginning in 2017. The use of these net operating losses may be limited in future periods.

Results of Operations

Comparison of Years Ended December 31, 1998, 1999 and 2000

Revenue. Total revenue increased by 532% from $120,000 in 1998 to $758,000 in 1999 and increased 47% to $1.1 million in 2000. The growth in revenue from 1998 to 1999 reflects the first full year of sales efforts following Webley's first Series A funding in July 1998 and a nonrecurring prepaid platform royalty of approximately $300,000. Above the nonrecurring prepaid royalty of approximately $300,000 in 1999, Webley grew revenue in 2000 through its expanded sales and marketing efforts in the Chicago local market and the improved productivity of our distribution channels, primarily resellers. Webley expects over 80% of its 2001 revenues will come from resellers and channel partners.

Costs of revenues. Costs of revenue increased by 410% from $184,000 in 1998 to $938,000 in 1999 and increased 49% to $1.4 million in 2000. The growth in cost of revenue from 1998 to 1999 includes $302,000 in platform costs associated with prepaid platform royalty. The remaining increase reflects the relocation of the Webley communications platform to two outside carrier-grade co-location facilities from server facilities internally located. The increase in costs of revenue in 2000 reflects an offset of the 1999 platform costs of $302,000 by an increase in co-location and fixed line costs caused by the separation of Webley from its former parent, Vail Systems, Inc., and the related benefits of Vail's in-house platform co-location and volume telecommunications contract commitments. In the fourth quarter of 2000, Webley was able to renegotiate more favorable telecommunications rates based on increased call volumes. Webley expects significant improvement in cost of revenues as a percentage of revenues in 2001 as fixed network and co-location costs are absorbed by increased subscriber revenues.

Operating expenses. Total operating expenses increased 145% from $5.3 million in 1998 to $13.0 million in 1999 and increased 60% to $20.7 million in 2000. These increases occurred in all categories of operating expenses over the three-year period as Webley grew its organization, and in 2000 included $2.6 million of sales and marketing

costs related to the Chicago local access campaign. Stock-based compensation charges were $5.1 million and $4.1 million in 1999 and 2000, respectively. These organization investments included the addition of 67 employees in 1999 and 39 employees in 2000.

Selling and marketing expenses. Selling and marketing expenses decreased 7% from $2.3 million in 1998 to $2.2 million in 1999 and increased 105% to $4.5 million in 2000. The modest decrease in selling and marketing expenses from 1998 to 1999 reflected the nonrecurring fourth quarter 1998 costs related to market trials in the San Francisco area and offsetting increases primarily from our investment in sales and marketing personnel. This investment included Chicago area direct sales staff added in the fourth quarter of 1999. The number of sales representatives increased from 4 in 1998 to 19 in 1999 (including 15 Chicago direct sales staff). Total sales representatives reached 38 in 2000 (including 28 Chicago direct sales staff). The $2.3 million increase in selling and marketing expenses from 1999 to 2000, was principally related to the Chicago area local access trial.

General and administrative expenses. General and administrative expenses increased 72% from $1.8 million in 1998 to $3.0 million in 1999 and increased 110% to $6.3 million in 2000. The increases from 1998 to 2000 were primarily due to additional infrastructure necessary to support the growing operations as well as the addition of senior level management and increased recruiting costs.

Research and development expenses. Research and development expenses increased by 380% from $458,000 in 1998 to $2.2 million in 1999 and increased 122% to $4.9 million in 2000. The increases over this period primarily represent investment in engineering and other technical personnel. Total engineering personnel increased from 8 in 1998 to 34 in 1999. In 2000, Webley initialized its own network operations center (NOC) on a 24/7 basis and continued to add engineering personnel to a total of 74 personnel. This increase from 1998 to 2000 was driven by the increased hiring of software developers, database administration, network and systems architects, product and project management, quality assurance and testing personnel and NOC staffing to develop, maintain and enhance our products.

Stock compensation. In connection with the grant of stock options during the year ended December 31, 1999, we recorded deferred stock compensation charges of $5.1 million. Stock compensation charges represent the difference between the deemed fair value for financial reporting purposes of our common stock on the date of grant and the exercise price of options granted to directors and employees to acquire common stock during this period, multiplied by the number of option shares and options issued to non-employees. We expect to record additional deferred stock compensation charges of approximately $4.1 million during 2000, and $5.5, $4.3 and $1.3 million for 2001, 2002 and 2003, respectively.

Interest and other income (expense). Interest and other income was $53,000 in 1998, $255,000 in 1999 and $770,000 in 2000. Interest expense was $109,000 in 1998, $526,000 in 1999 and $1,000 in 2000. The increase in interest income from 1998 to 2000 was the result of net increasing cash balances, due to the preferred stock financing raised in July 1998, August 1999 and March 2000. The increase in interest expense from 1998 to 1999 was primarily due to increases in debts payable under our line of credit and capital equipment leases. The decrease in interest expense from 1999 to 2000 was due primarily to the repayment of capitalized leases during the period. Other income includes rental income from the sublease of the company's former offices in Schaumburg, IL.

Liquidity and Capital Resources

Since 1997, we have funded our operations primarily through the private placement of common stock and convertible preferred stock totaling $41.3 million through December 31, 2000, and to a lesser extent, through bank borrowings and capital equipment lease financing. As of December 31, 2000, we had cash and cash equivalents of $7.8 million. Our operating activities resulted in net cash outflows of $3.5 million in 1998, $7.5 million in 1999

and $15.9 million in 2000. The operating cash outflows for these periods resulted primarily from our significant investment in research and development, sales and marketing and infrastructure.

To date, our investing activities have consisted primarily of purchases and maturities of short-term investments and capital expenditures for property and equipment, including $1.4 million of capital expenditures in 1998, $1.9 million in 1999 and $2.0 million in 2000. These capital expenditures have consisted primarily of computer hardware, software and furniture and fixtures for our growing employee base. We anticipate that investment in capital equipment will continue at an accelerated rate to maintain platform capacity consistent with expected subscriber growth.

Our financing activities generated cash of $6.6 million, $17.4 million, and $15.8 million in 1998, 1999 and 2000, respectively. Of these financing activities, the issuance of convertible preferred stock and common stock generated net proceeds of $5.6 million, $16.3 million, and $15.8 million in the same respective years. Convertible notes and the exercise of options generated net proceeds of $200,000, $2.1 million and none in 1998, 1999 and 2000 respectively. The Company had proceeds from bank borrowing of $928,000 in 1998. Repayment of bank borrowings and capital leases during the same periods were $91,000, $1.0 million and $31,000, respectively.

The Company believes that the net proceeds of this Offering, together with existing cash and cash equivalents, will be sufficient to meet working capital and capital expenditure requirements during the forecast period. (See "Use of Proceeds")

APPENDICES

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APPENDIX:

UNAUDITED AND AUDITED FINANCIAL STATEMENTS

Webley Systems, Inc.

Unaudited Financial Statements

The accompanying unaudited financial statements have been prepared in accordance with Generally Accepted Accounting Principles ("GAAP") and have not been examined, reviewed or compiled by the Company's independent certified public accountants. In the opinion of management, all adjustments considered necessary for a fair presentation have been included.

Webley Systems, Inc.

Balance Sheets

	Audited December 31, 1997	1998	1999	Unaudited Dec. 31, 2000
Assets				
Current assets:				
Cash and cash equivalents	-	$ 1,668,202	$ 9,659,016	$ 7,783,087
Accounts receivable	1,127	14,531	89,162	145,736
Prepaid expenses and other assets	9,366	54,093	68,981	82,093
Total current assets	10,493	1,736,826	9,817,159	8,010,916
Property and equipment, net	432,342	1,526,187	2,816,315	3,620,835
Other assets	22,949	48,712	140,762	357,390
Total assets	$ 465,784	$ 3,311,725	$ 12,774,236	$ 11,989,141
Liabilities and stockholders' equity (deficit)				
Current liabilities:				
Accounts payable	$ 92,418	$ 1,018,965	$ 639,400	$ 761,181
Accrued expenses and other current liabilities	110,635	236,254	591,922	770,255
Due to affiliates	604,223	707,731	710,597	12,480
Current portion of capital lease obligation	91,162	102,263	31,397	-
Current portion of line of credit	-	257,580	-	-
Total current liabilities	898,438	2,322,793	1,973,316	1,543,916
Capital lease obligation, less current portion	133,660	31,397	-	-
Line of credit, less current portion	-	669,708	-	-
Unsecured convertible notes payable	700,000	-	-	-
Stockholders' equity (deficit):				
Series A convertible preferred stock, $.001 par value; shares authorized, issued and outstanding 1997 to 2000, zero; 94,423; 94,580; 94,580, respectively	-	94	94	94
Series B convertible preferred stock, $.001 par value; shares authorized, issued and outstanding 1997 to 2000, zero; zero; 94,690; 176,507, respectively	-	-	94	176
Common Stock, $.001 par value; 1,000,000 shares authorized; shares issued and outstanding 1997 to 2000, 100,200; 140,597; 143,739; 144,109, respectively	100	141	144	144
Additional paid-in capital	104,897	7,209,967	38,205,934	64,910,446
Deferred compensation	-	-	(6,404,673)	(11,395,434)
Accumulated deficit during development stage	(1,371,311)	(6,922,375)	(21,000,673)	(43,070,202)
Total shareholders' equity	(1,266,314)	287,827	10,800,920	10,445,225
	$ 465,784	$ 3,311,725	$ 12,774,236	$ 11,989,141

Webley Systems, Inc.

Statements of Operations

	Audited Feb. 10 (inception) To Dec. 31, 1997	Audited 1998	Audited 1999	Unaudited 2000
		Year ended December 31,		
Revenues	$ 22,544	$ 119,998	$ 757,757	$ 1,113,606
Cost of revenues	70,193	183,967	937,591	1,397,175
	(47,649)	(63,969)	(179,834)	(283,569)
Expenses:				
Sales and marketing	258,930	2,318,540	2,153,748	4,473,423
General and administrative	676,616	1,762,967	3,024,239	6,349,316
Research and development	267,777	457,708	2,198,805	4,870,528
Stock-based compensation	-	457,117	5,052,508	4,094,959
Depreciation and amortization	80,722	307,442	541,790	948,200
Operating loss	(1,331,694)	(5,367,743)	(13,150,924)	(21,019,995)
Interest and other income	464	53,263	254,949	769,692
Interest expense	(40,081)	(108,973)	(526,101)	(1,141)
Net loss	(1,371,311)	(5,423,453)	(13,422,076)	(20,251,445)
Accrued convertible preferred stock dividends	-	(127,611)	(656,222)	(1,818,084)
Net loss applicable to common stockholders	($ 1,371,311)	($ 5,551,064)	($ 14,078,298)	($ 22,069,529)
Basic and diluted net loss per common share	($ 15.90)	($ 46.77)	($ 99.29)	($ 153.54)
Weighted average common shares outstanding	86,246	118,692	141,785	143,739

Webley Systems, Inc.

Statements of Stockholders' Equity (Deficit)

	Series A Convertible Preferred Stock Shares	Series A Convertible Preferred Stock Amount	Series B Convertible Preferred Stock Shares	Series B Convertible Preferred Stock Amount	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Deferred Compensation	Accumulated Deficit during Development Stage	Total Stockholders' Equity (Deficit)
Issuance of common stock in initial capitalization	-	$ -	-	$ -	95,000	$ 95	$ 902	$ -	$ -	$ 997
Issuance of common stock	-	-	-	-	5,200	5	103,995	-	-	104,000
Net loss	-	-	-	-	-	-	-	-	(1,371,311)	(1,371,311)
Balance at December 31, 1997 (audited)	-	-	-	-	100,200	100	104,897	-	(1,371,311)	(1,266,314)
Issuance of common stock upon conversion of Unsecured convertible notes	-	-	-	-	40,397	41	948,253	-	-	948,294
Stock based compensation	-	-	-	-	-	-	457,117	-	-	457,117
Issuance of Series A convertible preferred stock	94,423	94	-	-	-	-	6,009,930	-	-	6,010,024
Issuance costs of convertible preferred stock	-	-	-	-	-	-	(437,841)	-	-	(437,841)
Accrued series A preferred stock dividends	-	-	-	-	-	-	127,611	-	(127,611)	-
Net loss	-	-	-	-	-	-	-	-	(5,423,453)	(5,423,453)
Balance at December 31, 1998 (audited)	94,423	94	-	-	140,597	141	7,209,967	-	(6,922,375)	287,827
Exercise of stock options	-	-	-	-	3,142	3	199,997	-	-	200,000
Issuance of Series A convertible preferred stock, for consulting services	157	-	-	-	-	-	10,000	-	-	10,000
Deferred compensation on granted stock options	-	-	-	-	-	-	11,457,181	(11,457,181)	-	-
Stock-based compensation	-	-	-	-	-	-	-	5,052,508	-	5,052,508
Issuance of Series B convertible preferred stock	-	-	84,374	84	-	-	16,499,916	-	-	16,500,000
Issuance of convertible Series B preferred stock Upon conversion of unsecured notes	-	-	10,316	10	-	-	2,018,202	-	-	2,018,212
Issuance costs of Series B convertible preferred stock	-	-	-	-	-	-	(218,352)	-	-	(218,352)
Issuance of detachable stock warrants	-	-	-	-	-	-	372,801	-	-	372,801
Accrued Series A/B convertible preferred stock dividends	-	-	-	-	-	-	656,222	-	(656,222)	-
Net loss	-	-	-	-	-	-	-	-	(13,422,076)	(13,422,076)
Balance at December 31, 1999 (audited)	94,580	$ 94	94,690	$ 94	143,739	$ 144	$ 38,205,934	($ 6,404,673)	($ 21,000,673)	$ 10,800,920
Exercise of stock options	-	-	-	-	370	-	-	-	-	-
Stock-based compensation	-	-	-	-	-	-	9,085,720	(4,990,761)	-	4,094,959
Issuance of Series B convertible preferred stock	-	-	81,817	82	-	-	16,000,035	-	-	16,000,117
Issuance costs of Series B convertible preferred stock	-	-	-	-	-	-	(199,327)	-	-	(199,327)
Accrued Series A/B convertible preferred stock dividends	-	-	-	-	-	-	1,818,084	-	(1,818,084)	-
Net loss	-	-	-	-	-	-	-	-	(20,251,445)	(20,251,445)
Balance at December 31, 2000 (unaudited)	94,580	$ 94	176,507	$ 176	144,109	$ 144	$ 64,910,446	($ 11,395,434)	($ 43,070,202)	$ 10,445,225

Webley Systems, Inc.

Statements of Cash Flows

	Audited February 10, (inception) to Dec. 31, 1997	Audited Year ended December 31, 1998	Audited 1999	Unaudited 2000
Operating activities				
Net loss	($ 1,371,311)	($ 5,423,453)	($ 13,422,076)	($ 20,251,445)
Adjustments to reconcile net loss to net cash used in Operating activities:				
Depreciation and amortization	80,722	307,442	541,790	948,184
Stock-based compensation	-	457,117	5,052,508	4,094,959
Interest expense on unsecured convertible notes	18,768	29,526	77,212	-
Interest expense on unsecured convertible notes in connection with detachable stock warrants	-	-	372,801	-
Change in operating assets and liabilities:				
Accounts receivable, net	(1,127)	(13,404)	(74,631)	(56,574)
Prepaid expenses and other assets	(32,315)	(70,490)	(106,938)	(13,112)
Accounts payable	92,418	926,547	(299,515)	121,781
Accrued expenses and other current liabilities	91,867	144,387	355,668	178,333
Due to affiliates	604,223	103,508	2,866	(698,117)
Net cash used in operating activities	(516,755)	(3,538,820)	(7,500,315)	(15,675,991)
Investing activity - Purchase of property and equipment	(229,242)	(1,401,287)	(1,901,968)	(1,969,332)
Financing activities				
Line of credit advances	-	927,288	-	-
Pay-off of line of credit	-	-	(927,288)	-
Payment of capital lease obligation	(59,000)	(91,162)	(102,263)	(31,397)
Proceeds from sale of unsecured convertible notes	700,000	200,000	1,941,000	-
Proceeds from sale of Series A Convertible Preferred Stock, net	-	5,572,183	-	-
Proceeds from sale of Series B Convertible Preferred Stock, net	-	-	16,281,648	15,800,790
Proceeds from issuance of common stock	104,997	-	-	-
Proceeds from exercised stock options	-	-	200,000	-
Net cash provided by financing activities	745,997	6,608,309	17,393,097	15,769,393
Net increase in cash and cash equivalents	-	1,668,202	7,990,814	(1,875,930)
Cash and cash equivalents at beginning of year	-	-	1,668,202	9,659,016
Cash and cash equivalents at end of year	$ -	$ 1,668,202	$ 9,659,016	$ 7,783,087

WEBLEY SYSTEMS, INC.

Audited Financial Statements

Years ended December 31, 1999 and 1998 and period from February 10, 1997 (inception) to December 31, 1999 with Report of Independent Auditors

Webley Systems, Inc.

Audited Financial Statements

Years ended December 31, 1999 and 1998 and period from February 10, 1997 (inception) to December 31, 1999

Contents

Report of Independent Auditors

Board of Directors
Webley Systems, Inc.

We have audited the accompanying balance sheets of Webley Systems, Inc. at December 31, 1999 and 1998, and the related statements of operations, stockholders' equity (deficit), and cash flows for the years then ended and for the period February 10, 1997 (inception) to December 31, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Webley Systems, Inc. at December 31, 1999 and 1998, and the results of its operations and its cash flows for the years then ended and for the period February 10, 1997 (inception) to December 31, 1999, in conformity with accounting principles generally accepted in the United States.

Ernst & Young LLP

April 14, 2000,
except for Note 14, as to which the date is
December 1, 2000

Webley Systems, Inc.

Balance Sheets

	December 31 1999	December 31 1998
Assets		
Current assets:		
Cash and cash equivalents	$ 9,659,016	$ 1,668,202
Accounts receivable, net	89,162	14,531
Prepaid expenses and other assets	68,981	54,093
Total current assets	9,817,159	1,736,826
Property and equipment, net	2,816,315	1,526,187
Other assets	140,762	48,712
Total assets	$12,774,236	$ 3,311,725
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$ 639,400	$ 1,018,965
Accrued expenses and other current liabilities	591,922	236,254
Due to affiliates	710,597	707,731
Current portion of capital lease obligation	31,397	102,263
Current portion of line of credit	–	257,580
Total current liabilities	1,973,316	2,322,793
Capital lease obligation, less current portion	–	31,397
Line of credit, less current portion	–	669,708
Stockholders' equity:		
Series A convertible preferred stock, $.001 par value; 94,580 and 94,423 shares authorized, issued and outstanding, respectively	94	94
Series B convertible preferred stock, $.001 par value; 103,834 shares authorized; 94,690 and 0 shares issued and outstanding, respectively	94	–
Common stock, $.001 par value, 1,000,000 shares authorized; 143,739 and 140,597 shares issued and outstanding, respectively	144	141
Additional paid-in capital	38,205,934	7,209,967
Deferred compensation	(6,404,673)	–
Accumulated deficit during development stage	(21,000,673)	(6,922,375)
Total shareholders' equity	10,800,920	287,827
	$ 12,774,236	$ 3,311,725

See accompanying notes.